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The Unemployment Trust Fund and Reed Act Distributions

Updated September 12, 2012

Congressional Research Service

<https://crsreports.congress.gov>

RS22006

Summary

Under the Federal Unemployment Tax Act (FUTA; P.L. 76-379), the federal unemployment tax on employers finances the states' administrative costs of Unemployment Compensation (UC) and loans to states with insolvent UC programs. The extended benefits program is funded 50% by the federal government and 50% by the states, but the 2009 stimulus package (P.L. 111-5 §2005) as amended temporarily provides for 100% federal funding of this program through December 31, 2012.

FUTA tax revenues are placed into the Unemployment Trust Fund (UTF) that—among its many accounts—contains three federal accounts and 53 individual state accounts from the states' unemployment taxes. Under certain financial conditions, excess federal tax funds in the Unemployment Trust Fund (UTF) are transferred to the individual state accounts within the UTF. The transferred funds are referred to as Reed Act distributions.

The Reed Act, P.L. 83-567, set ceilings in the federal UTF accounts that trigger funds to be distributed to state accounts; Congress has changed these ceilings several times (P.L. 105-33, P.L. 102-318, and P.L. 100-203). There are other transfers in the UTF that are labeled by legislation as *special* Reed Act distributions. These are distributed in a manner similar to the Reed Act but do not follow all of the Reed Act provisions.

The most recent *regular* Reed Act distribution was \$15.9 million and occurred in 1998. The Balanced Budget Act (BBA) of 1997, P.L. 105-33, limited Reed Act distributions for the 1999 to 2001 period to *special* Reed Act distributions of \$100 million each year. In March 2002, the Job Creation and Worker Assistance Act of 2002, P.L. 107-147, provided for a one-time *special* Reed Act distribution of up to \$8 billion to state accounts.

The American Recovery and Reinvestment Act (P.L. 111-5 §2003) provided for a *special* UTF distribution that has some properties similar to a Reed Act distribution. The law distributes up to a total of \$7.5 billion to the states through a special transfer of funds from the federal accounts within the UTF to the state accounts, using the methodology required by the Reed Act to determine the maximum state allotments. Up to \$7 billion was distributed to states as incentive payments for changing certain state UC laws. Administrative funds totaling \$500 million was distributed among the state accounts, regardless of whether states changed their UC laws.

According to the Department of Labor, there is no projected *regular* Reed Act distribution through FY2021 on account outstanding loans in the UTF owed to the general fund of the U.S. Treasury.

This report will be updated if legislative activity affects Reed Act distributions.

Contents

What Is the Reed Act?	1
How Does the Release of Reed Act Funds Occur?	2
How Was the \$8 Billion Reed Act Distribution in 2002 Spent by the States?	3
Transfers to States in the 2009 Stimulus Package	4

Tables

Table 1. Reed Act Distributions.....	3
--------------------------------------	---

Contacts

Author Information.....	4
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What Is the Reed Act?

Unemployment Compensation (UC) is a joint federal-state program and is financed by federal taxes under the Federal Unemployment Tax Act (FUTA) and by state payroll taxes. The underlying framework of the UC system is contained in the Social Security Act: Title III authorizes grants to states for the administration of state UC laws; Title IX authorizes the various components of the federal UTF; and Title XII authorizes advances or loans to insolvent state UC programs. Among its 59 accounts, the federal UTF in the U.S. Treasury includes the Employment Security Administration Account (ESAA), the Extended Unemployment Compensation Account (EUCA), and the Federal Unemployment Account¹ (FUA); 53 state accounts;² the Federal Employees Compensation Account; and two accounts related to the Railroad Retirement Board. Federal unemployment taxes are placed in the ESAA, the EUCA, and the FUA; each state's unemployment taxes are placed in the appropriate state's account.

In law, the term Reed Act refers to a part of the Employment Security Financing Act of 1954, P.L. 83-567.³ This legislation amended Titles IX and XII of the Social Security Act (SSA) and established the basic structure of the UTF. The amendments to Title IX, among other things, provided for the transfer of excess funds in the federal portion of the UTF to the individual state accounts under certain conditions.

In practice, there have been two forms of Reed Act distributions. The first form, regular Reed Act distributions, follows the terms as set forth in the Reed Act. The second type, *special* Reed Act distributions, distributes some of the federal UTF funds to the states where these special distributions may follow some but not all of the conditions set by the Reed Act. The 1998-2002 Reed Act distributions were special distributions.

Federal law restricts states to using Reed Act distributions only to cover the cost of state benefits, employment services (ES), labor market information, and administration of state UC and ES programs. Suggested uses by the Department of Labor included establishing revolving funds for UC and ES automation costs, UC and ES performance improvement, costs related to reducing UC fraud and abuse, and improvement in UC claims filing and payment methods.⁴ An appropriation by the state's legislature is necessary before the state's share of this distribution may be used for UC and ES administrative expenses.⁵ Funds may not be used to extend a temporary unemployment benefit such as the Emergency Unemployment Compensation (EUC08) program.⁶

¹ The FUA is an account from which repayable advances are made to depleted state trust fund accounts to ensure that UC benefit obligations are met.

² The District of Columbia, Puerto Rico, and the Virgin Islands are considered to be states in UC matters.

³ The Reed Act was named for Representative Daniel A. Reed, who was chairman of the House Ways and Means Committee when the Employment Security and Financing Act passed.

⁴ U.S. Department of Labor, Training and Employment Guidance Letter No. 24-01, May 8, 2002, at http://ows.doleta.gov/dmstree/tegl/tegl2k1/tegl_24-01.htm.

⁵ See U.S. Department of Labor, Training and Employment Guidance Letter No. 18-01, April 22, 2002, Question and Answer 9, at http://ows.doleta.gov/dmstree/tegl/tegl2k1/tegl_18-01.htm.

⁶ For an explanation of the EUC08 program, see CRS Report RS22915, *Temporary Extension of Unemployment Benefits: Emergency Unemployment Compensation (EUC08)*, by Katelin P. Isaacs and Julie M. Whittaker.

How Does the Release of Reed Act Funds Occur?

Under FUTA, the federal tax on employers finances the states' administrative costs of UC and loans to states with insolvent UC programs. State UC payroll taxes finance the costs of regular UC benefits. The extended benefits program is funded 50% by the federal government and 50% by the states, but the 2009 stimulus package (P.L. 111-5 §2005) as amended temporarily provides for 100% federal funding of this program through March 7, 2012.

Under FUTA, employers pay a federal tax of 6.0%⁷ on wages of up to \$7,000 a year paid to each worker. The law, however, provides a credit against federal tax liability of up to 5.4% to employers who pay state taxes in a timely manner. Accordingly, in states meeting the specified requirements, employers pay an effective federal tax of 0.6%, or a maximum of \$42 per covered worker, per year.

At the end of the federal fiscal year, on September 30th, the net balance of the ESAA is determined. If the amount in this account exceeds 40% of the prior year's appropriation by Congress, then an "excess" balance exists. This excess balance is transferred first to the EUCA. When that account reaches its statutory maximum, the remaining excess balance is transferred to the FUA.⁸ *When all three accounts are at their statutory maximums*, any remaining excess balance is distributed to the accounts of the states in the UTF based on each state's share of U.S. covered wages. These distributions are called Reed Act distributions.

Reed Act distributions occurred in 1956 through 1958 and 1998 through 2002. **Table 1** lists the distributions. The most recent Reed Act distribution that was a *regular* and not a *special* Reed Act distribution was \$15.9 million and occurred in 1998. The Balanced Budget Act (BBA) of 1997, P.L. 105-33, limited the Reed Act distributions for the 1999 to 2001 period to *special* distributions of \$100 million each year. Any amounts in excess of the \$100 million that—absent the BBA amendments—would have been transferred to the states "shall, as of the beginning of the succeeding fiscal year, accrue to the federal unemployment account, without regard" to its statutory limit.

In March 2002, the Job Creation and Worker Assistance Act of 2002, P.L. 107-147, provided for a *one-time special* Reed Act distribution of up to \$8 billion to state accounts in the UTF, where the funds were distributed based upon the formula used for regular Reed Act distributions, using calendar year 2000 state information.⁹ The law labeled this transfer a "Reed Act" distribution although it differed from traditional Reed Act distributions, most notably because the law distributed a set dollar amount which was not determined by the statutory ceilings in the federal accounts and was distributed before the end of a fiscal year.

There was no Reed Act distribution in 2003, and no *regular* Reed Act distribution is projected through FY2021.¹⁰ According to the Department of Labor, there is no projected distribution through FY2021 on account outstanding loans owed to the general fund of the U.S. Treasury.

⁷ This does not include a 0.2% surtax that expired on June 30, 2011.

⁸ The statutory maximum for the EUCA is the greater of \$750 million or 0.50% of wages subject to state UC laws. The statutory maximum for the FUA is the greater of \$550 million or 0.5% of the covered wages.

⁹ For information on how states used the 2002 distributions, see General Accounting Office, *Unemployment Insurance: State Use of the 2002 Reed Act Distribution*, GAO-03-496 and GAO-03-567T, March 2003.

¹⁰ U.S. Department of Labor, Office of Workforce Security, Division of Fiscal and Actuarial Services, *UI Outlook FY 2012 Budget Midsession Review*, August 2012.

Table I. Reed Act Distributions

(\$ in millions)

Year	Reed Act Amount
1956	\$33.4
1957	71.0
1958	33.5
1998	15.9
1999 ^a	100.0
2000 ^a	100.0
2001 ^a	100.0
2002 ^b	8,000.0
2003	0.0
2004	0.0
2005	0.0
2006	0.0
2007	0.0
2008	0.0
2009	0.0
2010	0.0
2011	0.0

Source: CRS table created from U.S. Department of Labor, Employment and Training Administration data.

a. These distributions were set by the Balanced Budget Act of 1997.

b. This distribution was set by Job Creation and Worker Assistance Act of 2002.

How Was the \$8 Billion Reed Act Distribution in 2002 Spent by the States?

According to a General Account Office (GAO, now known as the Government Accountability Office) report, the \$8 billion Reed Act distribution reduced 2003 unemployment taxes in 22 states and UC administration costs in 17 states.¹¹ The Center for Employment Security Education and Research (CESER), a component of the National Association of State Workforce Agencies (NASWA), with the assistance of Booz Allen Hamilton and Decern Consulting, examined how states used the \$8 billion special Reed Act Distribution of 2002.¹² This study found that approximately half of the Reed Act distribution was used to lower state unemployment taxes in 2003 and 2004 from what they would have otherwise been. The special distribution also led to increases in spending on UC benefits, UC administration, and employment services.

¹¹ U.S. General Accounting Office, *Unemployment Insurance: States' Use of the 2002 Reed Act Distribution*, GAO-03-496, March 2003.

¹² *Unemployment Insurance: Assessment of the Impact of the 2002 Reed Act Distribution-Final Report*, Department of Labor, ETAOP 2004-11, released August 2008.

Transfers to States in the 2009 Stimulus Package

The American Recovery and Reinvestment Act (P.L. 111-5 §2003) provided for a special UTF distribution. The law provided a special transfer of UTF funds from FUA of up to a total of \$7 billion to the state accounts within the UTF as “incentive payments” for changing certain state UC laws. The maximum incentive payment allowable for a state was calculated using the methods also used in Reed Act distributions. That is, funds were to be distributed to the state UTF accounts based on the state’s share of estimated federal unemployment taxes (excluding reduced credit payments) made by the state’s employers. In addition, the act transferred a total of \$500 million from the federal ESAA to the state’s accounts in the UTF.

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